Executive summary

The EEB’s Environmental Fiscal Reform workshop covered two days of intensive discussions and brainstorming. Approximately 30 people attended the meeting on the first day, and on the second day there were about 25 participants. Participants ranged from officials from the Commission, OECD, Environment Ministries, and the European Environment Agency to NGOs from several Member States and Switzerland. The aim of the meeting was to identify instruments that can be used to facilitate the internalisation of external costs and push forward the idea of using economic/market based instruments for environmental purposes – to ensure internalisation of external costs – and facilitate a shift in taxes from labour to environmental pollution.

The Swiss NGO, NOE 21, premièred their short film CO2 Tomorrow I quit – highlighting everyday examples of how individuals can change their behaviour and choices to more sustainable ways. The film pushes forward the idea of environmental fiscal reform – using eco-taxes to reduce labour costs while maintaining revenue neutrality - this is potentially beneficial to the environment and the economy.

‘First time’ highlights dominated the first day presentations. From Commission representatives we learnt of reasons behind some (stalled) Commission documents e.g. the Communication on the Use of Market-based Instruments; and current developments and debates on a Green Paper on Market Based instruments; and an on-going review of environment state aid guidelines. A representative of the Finish Ministry of Environment made a first public presentation of an initiative for a new generation of environmental policies to be discussed under the Finnish Presidency, at the Informal Ministerial Council of July this year. The “Political Economy of Environmentally related taxes” is the title of an upcoming OECD report that was presented at this workshop. It showed that economic instruments can be used effectively for environmental purposes, without compromising the economy, under certain considerations. Political acceptance of economic instruments was said to be dependant on a number of factors. An EEB analysis of 25 National Reform Programmes (NRP) was presented for the first time. Only a few of the NRP focused attention on environmental tax reforms and the use of economic instruments for environmental purposes.

The second day consisted of a presentation by the European Environment Agency – on their “State of the Environment 2005” report and opportunities for
NGOs. Other discussions centred on a new initiative to promote the use of economic instruments in agriculture policy. ‘Climate related’ policies/topics such as the proposed CO2 passenger car taxation; updates on Kyoto flexible mechanisms, the EU Emission’s Trading Scheme and the Green Paper on Energy Efficiency were centre stage for the reminder of the meeting.

The broad range of issues discussed raised attention to some urgent and long-term issues of interest to the EEB EFR group. Upcoming initiatives such as the Green Paper on Market Based Instruments, the review of environment state aid guidelines and the Green Paper on Energy Efficiency, to name but a few, may offer possibilities to advance EU-level discussions on using economic/market based instruments for environmental purposes while forwarding the idea of shifting taxes from labour to resources use. Other initiative, such as the Finnish environmental policy initiative, and the use of institutional instruments such as enhanced co-operation and the open-method of co-ordination could be explored further. These can be used to advance an EU wide debate and action to facilitate environmental fiscal reforms and the shift of taxes from labour to environment/resource use. Other possibilities for action and conclusions are contained in a separate document.

The rest of this document gives a briefing into the presentations, discussions and first day conclusions. The results of the brainstorming event and NGO conclusions will be communicated to members of the working group separately.

**Agenda:** ANNEX 1

**List of participants:** ANNEX 2
DAY 1:

Meeting was opened by Stefan Scheuer.

Chair: Sören Dyk-Madsen, launches introduction round.

Progress and orientation of work in the European Commission regarding the selected topics:

Robin Miege DG Environment started by pointing out that the use of economic instruments is a flexible way for industry to respond to environmental objectives, to achieve efficiency and promote innovation. Eco-taxes may provide revenues and can lead to double dividend. According to observations made at the European Council meeting in Hampton court, 2005, over the past 15 years, taxes on labour in the EU have increased while taxes on the environment have remained the same. This year’s Commission’s Annual Progress Report on Lisbon, which is being prepared for the Spring Council, focuses on Lisbon’s National Reform Programmes (NRP). It is said that a number of Member States are promoting the idea of Environmental Fiscal Reform (EFR) in their NRP.

(Stalled) Communication on the Use of Market-based Instruments

Robin Miege informed that this Communication has been on the Commission’s work programme for two/three years, but is not yet out partly due to difficulties during inter-service discussions, and particularly between DG ENV and DG TAXUD. It was aimed to be a guide document for Member States on the use of market based instruments (MBI). In the meantime, some issues that were contained in the stated Communication have since been announced elsewhere, e.g. linking aviation in the EU Emission’s Trading Scheme (EU ETS), among others. In light of these developments, the Commission is reviewing the Communication and wants to make it into a Green Paper that would be prepared jointly between DG Environment and DG Taxud. Internal discussions are currently underway. It is felt that a Green Paper, being an open policy document, would launch an EU wide debate and provide opportunities to include more daring ideas. It is expected to be ready in April 2006. The Commission would consider the use of Article 96 of the Treaty - going over unanimity rules into qualified majority, as well as, the use of other instruments such as “enhanced cooperation”, to advance taxation debates in the Union. Border tax adjustments would also be considered for environmental purposes, specifically related to climate change. Revision of the Energy Tax Directive will be proposed by the Green Paper. The Green Paper would not be restricted to energy and transport, but would also consider the use of MBI in waste and biodiversity protection.
**Review of the environment state aid guidelines**

According to Robin Miege, the review process has started and is expected to be completed before end of 2007. This is done in the context of the new State Aid Action Plan (2005). DG Competition ran a public internet consultation last year that closed in mid-October. Analysis of responses is underway and results are expected to be released in March/April 2006. Issues that DG Environment is looking at are: possibility of using block exemption mechanism – would make it easier and more attractive for Member States to implement measures; how existing rules are still appropriate and whether they should be part of the block exemption; eco-innovation and research and development (R & D); internalisation of external costs etc. NGOs are invited to comments.

**Thematic Strategies and the use of market based instruments**

Robin Miege stated that Thematic Strategies do not specifically mention or recommend the use of market based/economic instruments but leave the door open for their use. Example, Clean Air for Europe programme (CAFÉ) mentions the inclusion of NOx trading at national level. The Pesticide Strategy will specifically mention using taxation to limit the use of pesticides. However, the Commission feels that introducing a pesticide tax at the present moment is immature, citing insufficient information on (certain) pesticides. The Commission might recommend the use of taxation on pesticides, in the future, once there is enough information on (existing) pesticides.

**Removal of environmentally harmful subsidies**

Robin Miege acknowledged that the removal of harmful subsidies is an important means to achieve environmental goals in the Union and fight against market distortions. At the same time, this is an extremely sensitive topic politically. OECD and EEA have addressed this issue and also published several reports on it. Most Member States are against addressing subsidy review/removal at the EU level. Reform of the Common Agriculture Policy (CAP) is looking at reforming agriculture subsidies at Community level, as a first step. In the energy sector, however, concerns on security of supply is very high, make any talk of removing subsidies to fossil fuel and nuclear industry even more difficult. The EU Sustainable Development Strategy (EU SDS) and Lisbon do mention removal of harmful subsidies, but, there is still a lack of commitment to address harmful subsidies at high political levels in some parts of the Commission and in Member States.

According to Manfred Rosenstock, even if the upcoming Green Paper on MBI mentions removal of harmful subsidies, there is not a strong legal instrument to achieve this.
Discussion:
The use of eco-taxes and the progress towards removal of environmentally harmful subsidies need high political level support to happen; this was the general central theme of the discussions. The 2003 European Council, under the Greek Presidency, had requested the Economic and Financial Affairs (ECOFIN) Council to make progress on tackling harmful subsidies, but there is still no clear indication of commencement of any technical work. Participants asked the Commission what type of institutional tools it intended to push forward to give an impetus to the use of MBIs such as eco-taxes, and the removal of environmentally harmful subsidies. The upcoming Green Paper on the use of Market Based Instruments (MBIs) is expected to address the choice of institutional tools. “Open method of coordination” was identified as an ideal institutional tool to deal with taxation, while “enhanced cooperation” was viewed as another alternative that would be addressed by the Green Paper. The need for long term, ambitious environmental policies was highlighted, and the barriers to environmental taxation discussed. In order to meet more ambitious targets, instruments should have low implementation costs. Barriers to EFR were addressed: main problem is that unilateral implementation is perceived by some national sectors as resulting in a loss of competitiveness, e.g. cement and steel industries. This may not be the case if the revenues are retuned to the same sectors. Tax revenues can also be used to reduce taxes for a country as a whole, but not all sectors would benefit.

It was proposed that NGOs focus on the reform of the environment state aid guidelines and try to influence the application of adequate rules – using this as a means to facilitating the removal of harmful subsidies. NGOs could also work towards removal of environmentally harmful state aid by focusing on other state aid guidelines such as research and development guidelines, and push for changes, including promoting eco-innovation. The push for using market based instruments can be linked with enforcement of legislation; for example, the Commission could focus on using urban action plans to reduce air pollution as a means to secure enforcement of the Air Quality Directive.

The (stalled) draft Directive on the relation between energy taxation and emission trading

Robin Miege started by giving background information to the Energy Products Tax Directive that entered into force at the beginning of 2004. This Directive is not considered an ideal instrument from a climate change perspective: generally the agreed minimum energy tax rate is lower, than would be preferred by environmentalists, with too many exemptions. Additionally, it is a product tax and
not explicitly CO2 taxation tool - although it can give incentives for CO2 reductions; and covers some sectors that are not covered by the EU ETS. For ‘internalisation of external costs’ there is a need for stronger tax harmonisation, indexation and complementary increase in minimum rates. When the Commission proposed such measures, it was met with strong resistance from Member States and the European Parliament, therefore, it withdrew the Directive, hence it took over 6 years for an agreement to be reached – and the result was the very low minimum rates and other exemptions, which, from an environmental perspective are considered unfavourable.

Emissions trading: review of EU ETS is important for post-2012, when Kyoto targets would be reviewed. Some important questions to consider include: is there a need for harmonised rule? How to treat new entrants/closures? Etc. In mid-2006, the Commission will report to the Council on results of the first trading period. The Communication for the second National Allocation Plans (NAP II), containing drafting guidelines for Member States was adopted in December 2005.

On the relationship between energy taxation and EU ETS: the main concern is the issue of double burden and what to do about it. Energy taxation is a product tax and not an emissions tax.

On including aviation in the EU ETS: European Commission published a communication on Reducing the climate change impacts of aviation, on September 27, 2005. Within the context of this Communication, the Commission will make a legislative proposal by the end of 2006/7. A Working Group proposed under this Communication will deal with design issues of how to include aviation in the EU ETS – two NGOs sit on this WG. The airline industry prefers inclusion of aviation in the EU ETS.

Discussion:
Discussions centred on identifying obstacles to energy taxation and finding ways around them. The current high energy taxes were a stumbling block for political leadership on energy taxation in the Union. Despite this, the need to argue that there is a rationale for energy taxation was emphasised. On the NAP I experience: this was a pilot phase and the idea was to have a system that works, however, the same excuse would not hold true for NAP II. Most Member States have done their NAP I allocations in an un-harmonised manner making comparisons between Member States rather difficult. Negative predictions that prices would fall during the first allocation period, have not happened. Montreal decisions are giving new perspective for stricter targets and further strengthening of instruments and more stringent commitments beyond 2012.

New guidance of NAP II drafting suggests a more harmonised approach of allocation, and sticking to Kyoto target is emphasised.
Implementing of existing legislation on natural resources was an issue that highlighted as lagging behind, by a participant. The Commission reiterated the importance of implementing existing legislation as a priority, for which the Commission’s services will work in collaboration with Commission’s Legal Unit.

**Smart, Sustainable and Solidarity – A new generation of Environmental Policy**

Tania Nikula presented a new initiative, for the Informal Ministerial Council in July 2006, under the Finnish Presidency of the EU. Still in its developmental phase, this was the first public audience and a proposal for a meeting in the spring to discuss ideas was put forward. The presentation presented the current state of environmental policies in the Union. It pointed out to strengths, weaknesses, opportunities and threats of environmental policies in the Union. The strengths identified are: success in reducing emissions (e.g. lead, CFCs, NOX), and the fact that the EU is seen as a frontrunner in environmental policy worldwide. The main weaknesses of current environmental policies were identified as: present environmental policy is simply ‘buying time’ – making it possible to keep on polluting; it focuses on ‘end-of-pipe’ approaches – this is insufficient and not beneficial in environmental nor economic terms; it fails to reward efforts to save natural resources; it does not focus on the life cycle approach. Another weakness is the rigidity of EU regulation – a more flexible regulation would allow for better working with and within Member States, possibly promoting “enhanced cooperation”. In some cases a bottom down-approach would benefit the environment. The presentation identified existing opportunities as: those that promote ‘win-win’ solutions, environmental technology transfers and innovations; stating that new modes of production would benefit certain sectors. Current threats were indicated as: climate change, consumerism and increasing transport, overuse of resource, and contradictory policies at EU level.

The presentation went on to identify the possible options for the future of environmental policy in the EU (BOX1) and a possible roadmap to achieve them (BOX 2). In general, better and smarter policy making needs economic instruments and more dialogue with a cross-range of stakeholders. Targets for material use and energy efficiency, for example, and means for Member States to achieve them are other requirements identified.
Discussion:
Discussions centred on the need for a stronger focus on enforcement; and debated the use of voluntary ‘soft tools’ versus mandatory approaches; and whether to focus on ‘willing’ sectors or cut across all-sectors. There was a call to the Finnish Ministry of Environment (MOE) to make this environmental initiative more ambitious - aiming higher, and using the Millennium Ecosystem Assessment as the context within which such an initiative should be based; in consultation with civil society and taking such views into consideration. The Finnish MOE has identified the food and construction sectors as sectors that they would initially focus on. In order to achieve enforcement of legislation, some participants were in favour of focusing on all sectors, while others pointed to international sectors such as the car industry as vital. Voluntary approaches were criticised by some participants, while caution was expressed on any indiscriminate use of targets. Dialogue between different actors and stakeholders, was identified as a possible way forward to interface environment issues into other policies.

The Political Economy of Environmentally Related Taxes
Nils-Axel Bratthen gave an insight into an up-coming OECD report on environmentally related taxes, which will be issued later in the year. The study draws on information contained in an OECD database on instruments used for environmental policy, including findings of work on instrument mixes, and additional literature searches; as well as a large number of case studies. Examples of environmentally-related taxes in use in the OECD countries were given. In all countries, the tax rates of petrol were shown as higher than those of
diesel. This is a problem given the environmental externalities of diesel.

Interestingly, Turkey was identified as a country paying most petrol and diesel taxes in OECD countries – generally poor people do not have cars in Turkey, so such taxes are aimed at the rich. The analysis took a closer look at the UK tax rates, showing that applying high tax rates on diesel with high sulphur content (50 mg/km fuel) created a negative supply side reaction. In general, studies on fuel prices, taxes and fuel use in OECD countries show that price mechanisms do work – increase in petrol prices showed a decrease in the use of petrol. Studies on sectorial competitiveness in the cement and steel sector in OECD countries, showed that introduction of a tax on these sectors has a positive environmental impact, but can have negative impacts on the sectors. This can be reduced by recycling the taxes back to the sector (which is likely to reduce the environmental effectiveness of the policy). Another way to reduce negative impacts in the sectors is to use Boarder Tax Adjustments. These studies also showed that in spite of some carbon leakage, it is possible to achieve global reductions in CO2 emissions.

Ex-post studies on sectoral competitiveness using empirical country studies of implementation of environmental policies show the need to adequately assess and address competitiveness pressures and highlight the need to ensure that mitigation measures do not reduce abatement costs. Additionally, countries should strive for the broadest possible tax bases to achieve cost-efficient emission reductions. A gradual phase in of taxes is recommended as a way to soften the impact and give companies time to adjust to new tax measures.
On the effects of environmental taxes on income distribution, most studies show a regressive direct impact, which is reduced by indirect effects of environmentally related taxes. The studies recommend addressing the distributional effects, through mechanisms in the decision-making process. “Mitigation” measures are said to reduce the environmental effectiveness of taxes; so preference should be on “compensation” measures that maintain the price signal of the tax.

On administrative costs – it is possible to design a number of instruments for environmental policy with relatively low administrative costs. However, many instruments used for environmental policy include a large number of ‘special provisions’ – often introduced for non-environmental reasons; and these - greatly increase administrative costs.

The study also found that the acceptance of an economic instrument seems to be related to the degree of awareness of the environmental problem the instrument is to address. The recommendation is thus to “prepare the ground” for later instrument implementation by providing correct and targeted information to the public. The degree of political acceptance also depends on, the perceived ‘fairness’ of the instrument in question. Political acceptance could be strengthened by creating a common understanding of the problem at hand, its causes, its impacts, and the impacts of possible instruments e.g. by involving relevant ‘stakeholders’ in policy formulation.

The study found that effective and efficient instrument mixes require a good understanding of: the environmental issue to be addressed; the links with other policy areas; and the interactions between the different instruments. Examples of interactions between instruments are given below in BOX.

The main conclusions of the study are:

- environmentally related taxes can be effective and efficient instruments for environmental policy;
- the environmental effectiveness and economic efficiency of the environmentally related taxes applied in OECD member countries.
could, however, be improved further if existing exceptions and other special provisions included in the taxes were scaled back

- And if the tax rates were better aligned with the magnitude of the negative environmental impacts to be addressed.

Future and on-going work of the OECD focuses on is analysing

- Impacts of environmentally related taxes and emission trading systems on innovation.
- Comparison of second-best taxes (with exemptions, etc.) and second-best (grandfathered) trading systems.
- Study of impacts of variable waste collection charges. (Soon ready.)
- Additional improvements to the database.

Discussion:

Discussions focused on national examples were EFR was being applied in some countries – in some cases such as Germany and UK, Denmark, Norway, fiscal revenues have been used to reduce social costs. Participants elaborated further on the effects of taxation in different sectors. Promoting taxation within EFR – as revenue neutral - was identified by participants as the best possible way to achieve political acceptance at the national level. Others expressed the need to be vigilant on sectors that may use money from tax revenues in ways that will result in negative environmental impacts.

**Screening 25 National Reform Programmes on economic Instruments – a first draft**

Maria Butenkamp presented a draft of an analysis carried out by herself and Pendo Maro, on the Lisbon National Reform Programmes that Member States had to hand to the Commission in October 2005. In general, the plans were found to be of differing quality. Some of the general comments that apply to the majority of the NRP include: that most plans were incomplete, with vague objectives, timetables, budgets and milestones; environmental tax reforms and economic instruments were present in some countries (e.g. Malta to build capacity to ‘introduce polluter pays principle’; fiscal/ financial incentives for cleaner/ more efficient vehicles: Belgium France, Luxembourg, Italy, Portugal, Sweden; financial incentives for renewable: France, Greece, Ireland, Luxembourg, Sweden, Malta) and reform of harmful subsidies was mentioned a only a few of them (e.g. Luxembourg to analyse subsidies energy sector; Netherlands and Cyprus to revise subsidies; Slovenia will apply environmental criteria as well as review resources/waste subsidies); infrastructure/transport charging was also in some countries (e.g. Netherlands: considering kilometre levies, France & Czech R: pricing to pay
roads; Sweden and Ireland considering road charging. Stockholm: congestion tax trial; Germany road charging for heavy vehicles; Sweden considering new tax on air travel passengers in 2006.). Further analysis of these findings and a report will be presented at the March 6th joint EEB-ETUC-Social Platform Conference on Lisbon.

Discussion:
Discussions focused on NGO involvement in the NRP process at the national level. An Estonian NGO representative stated it was the first time that NGOs have been involved in the preparation of NRP and that they had received very good feedback from their government. This was not always the case from the other countries. It was noted that although all countries in the EU are supposed to have a National Sustainable Strategy, it was not always mentioned in the NRP. As a follow-up to the NRP most countries would have to write a progress report to the Commission in a year’s time – EEB members were urged to keep watch of this process and get involved.

Conclusions of first day
In conclusion, Stefan Scheuer acknowledged the broad range of issues discussed, and then gave his personal impression and summary of the day. He noted that environmental fiscal reforms and eco-taxes are being discussed at the EU level, including by heads of states, but progress on moving forward with implementing EFR is still lacking. The upcoming Green Paper on Market Based Instruments, may offer some hope in advancing an EU wide debate that would give a boost to EFR and removal of environmentally harmful subsidies. He reiterated the call for NGOs to get involved and give input to the environment state aid guidelines. On the implementation of the 6th Environment Action Plan (6EAP) and the seven Thematic Strategies, proposals for using MBIs are so far absent except for the rather obscure emissions trading for NOX. On enforcement, he urged the Commission to push Member States to use more MBI before considering flexibility e.g. in air quality standards, the Commission should insist on the use of MBIs. He thanked the Finnish MOE representative for presenting their draft ideas on the new environment policy initiative and the role of fiscal instruments – highlighting the need for the initiative to be more ambitious. He thanked OECD for presenting their upcoming report. Finally, he stressed the need to improve communication between economists and environmentalists at the national level so as to bring together the different objectives of sustainable development.
Day 2

**CO2 based taxation on cars**

**Aat Peters** presented the European Parliament’s (EP) resolution of 2003 and an EU Commission proposal of 2005 that address CO2 based taxation of passenger cars. He presented the EP resolution’s three pillars for action as: a target for entire fleet of all new cars put on the market in 2010 must on average be 120 gCO2/km; consumer information on cars should include fuel efficiency and emissions; taxation of cars to be harmonised.

Three elements of the Commission’s 2005 proposal: abolition of car registration taxes in five to ten years; a refunding mechanism while abolition is pending; a CO2 element in tax base of circulation. The general difficulty is that many countries do not want to give up registration tax and that taxation requires unanimity, so one country is enough to block an EU wide tax initiative in the Council.

The first country in the EU to introduce a CO2 based car tax was the UK, in 2001. It also introduced a CO2 based differentiated tax for company-cars that has resulted in companies using smaller cars in the UK, compared to the situation in most other Member States. This example show that car taxation does work.

Recommendations:
- Keep registration tax
- Use strongly progressive rate of CO2 based tax and introduce it for company cars as well
- Align taxation with labelling so consumers are aware

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**The use of Economic Instruments in Agriculture Policy**

**Arjan Berkhuysen** presented the results of a study (commissioned by his organisation) on the potential use of economic/fiscal instruments in the agriculture and food sector. A big problem in agriculture is that sustainable food is more expensive because conventional agriculture – that uses commercial fertilisers and other non-sustainable inputs - is subsidised and its environmental externalities are not accounted for in the final price of products. There is a need to define a long-term strategy on how to get environmentally-related taxes at EU level. In the agricultural sector, two areas to focus on for possible application of economic/market based instruments are inputs and emissions: e.g. fertilizers, pesticides and water are most relevant to be taxed. He pointed to possible strategic options as: learn from case studies where such taxes on agriculture sector have been successful and where not; improve general support for ecological tax reforms – convince public and focus on Green Paper on MBI from
Commission (how to strengthen EFR); go after specific results; advocate an EU wide pesticide tax.

Some participants advocated for the introduction of a product-side tax differentiation between (green) labelled and non-labelled products (like reduced VAT). While others felt that agriculture nutrient leakages should be targeted through the use of a fertiliser tax – which is essential for implementation of the Water Framework Directive goals. The main issue is still how to abolish all environmentally harmful subsidies to the agriculture sector.

**Internalisation of external costs: Kyoto flexible mechanisms and EU Emissions Trading System**

**Ruta Rubniene** started by presenting the outcome of the international COP11/MOP1 that took place in Montreal in December 2005. Agreements were reached on starting negotiations on a new round of emission reduction targets for the second commitment period of the Kyoto Protocol (2013-2017) - to ensure the continuity of carbon markets, and to allow governments to put policies and measures. Other agreements at Montreal included: a decision to (at COP2, 2006) reviewing and improving the Kyoto Protocol; a Five Year Plan of Action on Adaptation, to assist least developed countries to cope with the impacts of climate change; and approval of the Marrakech Accords (making JI, ETS operationalized).

Agreements were also reached to strengthen the Clean Development Mechanism (CDM).

NGOs were urged to keep track of the following issues: additionally – there is a need to ensure that additionally is not weakened; Carbon Storage and Sequestration – submit a proposal on how NOT to include CCS projects in CDM. JI is a priority to be lobbied at the EIT countries – to which NGOs from these countries were encouraged to follow the progress within the respective national governments, and monitor bilateral agreements regarding Green Investment Schemes (GIS), so that revenues are earmarked to combat climate change. GIS are project based international emission trading mechanism based on earmarking revenues of hot air trading for climate change or other environmental purposes – they are considered an alternative for JI in Bulgaria, Romania and Russia; and considered an alternative for CDM/JI credits for buyers in: Austria, the Netherlands, Canada, Japan.
An EU perspective:
The NGO views presented by CAN-Europe expressed the need for the second phase of the European Climate Change Programme (ECCP) to include: a goal for a 30% emission reduction by 2020; strengthening national implementation of existing policies (EU ETS and Renewables Directive); avoid locking Europe into high-carbon or high-risk technologies; avoid over-reliance on external credits – domestic action first. The first phase of the EU Emissions Trading Scheme was said to have not resulted in any environmental benefits thus far (BOX), and that half of the countries were not on track to meet their Kyoto targets (BOX). For the second phase of the EU ETS, reductions over the current level are required and the lack of a Kyoto constraint should not be used as an excuse for over-allocation.

Incentives: EU ETS does not provide enough incentive to long term investments for industry

Targets: reductions only vis-à-vis BAU projections for the future, increases over recent years - threaten Kyoto targets

Rules: little use of auctioning

Domestic action: worrying trend to rely on JI/CDM for Kyoto compliance - supplementarity?

Transparency: Lack of access to the process and no independent assessment of data for projections/allocations

No environmental benefits so far – Future improvements are necessary!

Half of countries are not on track to meeting their Kyoto targets, but only two of EU MS (DE, UK) require reductions by the year 2007 against the base years’ period.
On including aviation in the EU ETS:
The aviation sector has received historic privileges on fuel taxes and on international tickets. It is exempted from Kyoto Protocol emission scheme and it is a sector that does not face similar competitive constraints as other sectors such as stationary emission source sectors (e.g. steel). The Communication Reducing the climate change impacts of aviation identified the following as options for ‘internalising external costs’ of the aviation sector:

- Fuel taxation – opposed by politicians
- Emission charges – opposed by industry
- Emissions trading
  - Environmentally and economically efficient (taps cheapest reduction potentials, environmental outcome certain)
  - No explicit references in Chicago convention, bilateral air service agreements etc. (less legal constraints)
  - Preference of airline companies and strongly supported by airport companies.

The aviation Working Group under the ECCP started working on the technicalities of including aviation in the EU ETS in late autumn 2005. The results of this group are expected by 30 April 2006.

In order to address all contributing factors of the aviation sector within the EU ETS a package of measures is advocated one that adheres to the following conditions:

- **End privileged treatment** through other policies and link to EU ETS, aiming for harmonised rules and central administration
- **Equal efforts**: aviation must contribute to at least similar reductions compared to other sectors (EU target -8% from 1990 levels)
- **All impacts to be addressed**: distinct package of measures for all impacts - integrate more than CO2 (other emissions) in EU ETS
- **Maximum scope**: widest geographical coverage (all flights departing and landing in the EU)
- **Full internalisation** of climate impacts: every ton of CO2 emission must get a price tag – using auctioning to disseminate allowances.

Some participants suggested the use of a ticket tax – something which is strongly opposed by the aviation sector because of fears of the effects a price increase might have. Others felt that a ticket tax would not necessarily act as an incentive for aviation companies to switch to less polluting aircrafts. A participant suggested challenging the aviation sector through the World Trade Organisation (WTO). It was made apparent that this was not an issue for WTO but for the International Civil Aviation Organisation (ICAO), and that EU’s earlier attempts to challenge aviation fuel tax exemption via ICAO had failed.
**The European environment – State and outlook 2005: Brief presentation**

**Jock Martin** gave a brief presentation of the third EEA European Environment state and outlook 2005 report. As part of its mandate, the EEA makes a comprehensive review of the state of the European Environment every five years; the previous report was in 1999. The 2005 report can help the EU in its mid-term evaluation of the union’s 6th environmental action programme and the EU’s sustainable development strategy. The 2005 edition covers the enlarged EU and contains several new features such as the core set of indicators and the country by country comparisons analysis - it was released in November 2005. The report shows that past EU legislation on environment has worked and cost-effectively, reducing many air and water emissions and increasing waste recycling – though effects take a long time to be noticed, sometimes decades. However, most of the success has been on point sources of pollution, with diffuse sources of pollution still not very well addressed. Shared learning on implementation can further enhance effectiveness of implementation.

The most startling conclusion is that Europe’s ecological “footprint” is more than double the capacity of its natural resources. This means that it takes five hectares of land area to produce the resources an EU citizen consumes and to absorb the wastes s/he generates. This is more than Japan and half that of the United States, but more than double that of countries like Brazil, China or India.

Areas that most threaten environmental progress are: Land use, consumption and trade patterns. Specific problems are increasing urbanisation and abandoning of land, climate change, slow progress on energy demand management, and depletion of natural resource – over fishing, possible biodiversity loss, soil erosion etc, and water stress. The presentation makes the following recommendations (BOX)

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**Report will be translated into all EU languages by the end of 2006.**
EEA technical report no 8/2005 Market-based Instruments for Environmental Policy in Europe is available after 26th of January via their website. On January 26, the report “Using the market for cost-effective environmental policy” (EEA Report No 1/2006), was published at [http://reports.eea.eu.int/eea_report_2006_1](http://reports.eea.eu.int/eea_report_2006_1)
The report "Market based instruments for environmental policy in Europe" is a longer version of this new report.

EEA has a number of MBIs- related policy analyses on the pipeline for 2006. One of these is the analysis of EFR experience in EU MS, specifically looking at environmental benefits combined with competitiveness and demographic changes, to start in June 2006.

**Green Paper on Energy Efficiency**

Lars Frieberg started by pointing out that energy dependency in the EU-25 is 50% and will reach 70% (import of gas 80%, oil 90%) by 2030, so there is a need to address the demand side of energy policy. He noted that Energy Commissioner Piebalgs sees energy efficiency as a priority, given its enormous potentials (BOX). Energy efficiency could potentially result in energy saving of 20% by 2020, making a saving equivalent to 60 billion EURO per year (equivalent to the energy use of Finland and Germany) and the creation of about a million jobs. However, such a potential is not realised due to financial and regulatory obstacles; lack of market for energy efficiency; prices not transparent and cost effective; lack of information and education, to name but some.

The main regulatory obstacles are: reluctance to commit to targets and sub-optimal use of tax and state aid. To counter these obstacles policy makers need better information, political will and awareness; better use of tax and state aid and a rationalisation of subsidies. Some proposed solutions for the transport sector are: traffic management (Open Sky – air traffic control (6-12% less fuel), GALILEO EU GPS system); penalise fuel guzzlers/de-tax cleaner vehicles; public procurement obligations to favour and promote energy efficiency; restricting access and zoning in urban areas; use of economic instruments such as congestion/road charges and including aviation in the EU ETS. For the household sector, the Energy Performance of Building Directive needs vigorous implementation, coupled with
the use of Energy Performance Certification. This Directive should extend obligations for renovations of buildings to cover those below 1,000 square metres. The use of appliances that are energy efficient, such as LED lamps is encouraged; the Eco-Design Directive could also play an important role here.

The Commission launched a consultation on the Green Paper to which Member States gave their views in October 2005. In the meantime, the Commission has started drafting its ‘practical action’ proposals before the end of consultation on March 31, 2006. The Consultation is based on 25 questions – giving a possibility to comment on all areas of Energy Efficiency.

A new Green Paper on Security of Supply is to be produced in the early part of 2006 – it will focus on oil, coal and nuclear, not energy efficiency.

**EU Water Policy and Economics**

**Stefan Scheuer** started by pointing out the overall objective of the EU water policy – the Water Framework Directive 2000 (WFD) as: to achieve good status of all waters by 2015; to prevent further deterioration and to phase out hazardous chemicals and minimise pollution. It is the first ever legislation with an ecosystem based approach despite its many exemptions and long deadlines. To achieve the objectives, the WFD proposes to use tools such as polluter pays, river basin approach to management, and water pricing. Despite its ambitious start, implementing the WFD is facing increasing opposition from Member States such as Finland, Denmark and the Netherlands mainly from the following sectors: navigation, hydropower and agriculture. Additionally, data on most waterways is missing and most waters are at risk to fail the WFD’s objectives.

Article 5 of the Directive addresses cost recovery of water services including environmental and resource costs. Currently EEB is conducting a survey focusing on the quality of the economic analyses reported by Member States - within River Basin Management Plans in different countries. Preliminary results have identified good and bad cases (France and Hungary - good; Netherlands and Spain - bad).
In order to achieve the objectives of the WFD, there is need for proper economic appraisals, addressing diffuse impacts and using water pricing. MBI/economic instruments that are proposed to use are: charges for irrigation and nutrient losses (e.g. in Netherlands farmer pays extra fee if fertilisers used exceeds agreed level kg/ha for soil type).

EEA is currently developing capacities to evaluate/audit status of water bodies at European level – this also involves the development of environmental accounting techniques by the EEA, to allow better water management by river basin authorities.

By Pendo Maro.
With contributing notes from Valdur Lahtvee (Estonia).
ANNEX I

Draft Agenda

DAY 1 – Chair: Sören Dyck Madsen (The Ecological Council, Denmark)

9.15: Welcome and introduction by Stefan Scheuer (EEB Policy Director)

9.30: Progress and orientation of work in the European Commission regarding the following:
- the (stalled) Communication on the Use of Market-based Instruments
- the Thematic Strategies and upcoming review of the 6th Environment Action Plan (EAP)
- the forthcoming review of the environmental state aid guidelines

Presentation by Robin Miege DG Environment

Discussion

11.00: Break

11.30: Progress and orientation of work in the Commission regarding the following:
- the next phase in Emission Trading/how to include aviation in emission trading
- the (stalled) draft Directive on the relation between energy taxation and emission trading

Presentation by Robin Miege, DG Environment

Discussion

12.30: 6th EAP Review and EFR – Introduction and discussion of proposal for a new environmental initiative from the Finnish Presidency – Presentation and exchange of ideas by Taina Nikula, Ministry of Environment, Finland

Discussion

13.30: Lunch (Interlude: 12 minute EFR film, by Noe 21)

14.45: OECD presentation on the political economy of economic/tax instruments, by Niels-Axel Braathen (OECD)

Discussion
15.30: Lisbon National Reform Programmes and EFR – Introduction and analysis by Maria Buitenkamp, Stichting Natuur en Millieu, Netherlands

Discussion

16.00: Conclusions of day 1 – by Stefan Scheuer

17.00: End of day 1

DAY 2

10.00: Welcome and objectives of the day

10.15: CO2 passenger car taxation
Aat Peters, T&E to introduce the topic: brief overview of what is happening at the EU level and what is on the agenda; potential way forward for NGOs e.g. what can be done at national level? Distil ideas for EU actions

10.45: The use of economic instruments in agriculture policy
Presentation and discussion: new report on the potential of other economic/financial instruments than subsidies for the agriculture and food sector; by Arjan Berkhuysen, Stichting Natuur en Milieu

11.15: Aviation, emissions trading and climate change
Presentation by Ruta Rubniene, CAN-E on what has happened at EU level and what is relevant for the national level actions – opportunities for 'internalisation' of external costs)

BREAK

11.45: The European Environment: State and Outlook 2005 - a message on tax reforms
An evaluation of environmental tax reforms in EU 25. Presentation and discussion by Jock Martin, EEA

12.20: Energy Efficiency
Introduction to the Green Paper on Energy Efficiency – why it is relevant and how we want to shape it, if we do – some of the 25 questions could form a basis for discussion; also what it says about energy efficiency and possible measures in other sectors such as transport, including aviation, household etc – opportunities for NGO actions on internalisation of external costs. By Lars Friberg, CAN-E

12.50: EFR Film
Presentation and discussion by Chaim Nissin, Noe 21

LUNCH

14. 10: Water Framework Directive
Water pricing to support ecological objectives; economic analysis, cost-effectiveness is the starting point but it is done badly or not at all in most Member States; NGOs lack capacity – what can EFR do about this? **By Stefan Scheuer**

14. 40: Brainstorming and Conclusions by Stefan Scheuer

16. 00: END
ANNEX 2
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EEB WORKSHOP ON ENVIRONMENTAL FISCAL REFORM
January 13-14, 2006

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